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North Continental Energy Ltd.

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1987 ANNUAL REPORT

CORPORATE INFORMATION

REGISTERED OFFICE:

104, 1410 Mayor Magrath Drive
Lethbridge, Alberta
Canada T1K 2R3
Phone (403) 328-4010

LEGAL COUNSEL:

Huckvale & Co.
612 - 3rd Avenue South
Lethbridge, Alberta
Canada T1J 4A2

AUDITORS:

Munton/Anderson
200, 1410 Mayor Magrath Drive
Lethbridge, Alberta
Canada T1K 2R3

TRANSFER AGENT:

Central Trust Company
401 - 8th Avenue S.W.
Calgary, Alberta
Canada T2P 1E4

STOCK EXCHANGE:

Alberta Stock Exchange
Trading Symbol – NCL

BANKER:

Bank of Montreal

North Continental Energy Ltd.

PRESIDENT'S REPORT

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To the SHAREHOLDERS:

During the past year our Company has participated in the drilling of four wells and has acquired a 10% interest in 1,920 acres of freehold leases in Southeast Saskatchewan. Two of the wells, (1-28-9-1 W2M at Whitebear, SK) and (12-34-4-34 W1M at Hastings, SK) are now on production and a third well, (16-26-4-2 W2M at Alameda, SK) shows some potential and will undergo further testing. The other well was drilled near Warner, Alberta and was abandoned because of water problems.

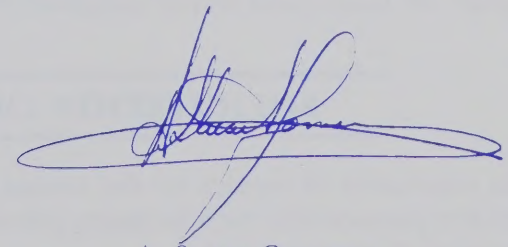
Revenue from the new wells will begin early in 1988. Our share of recoverable reserves from this recent drilling is estimated to be 31,000 barrels. Potential is high for finding additional reserve on these leases. The next well in our program will be drilled in the second quarter, 1988.

Recent drilling developments in the Black Butte area have caused us to delay the drilling of a well until our geological studies have been updated.

Because of the mild weather, our gas production at Hanna has been lower than usual this winter and will result in lower revenues.

We anticipate that our participation in Southeast Saskatchewan will gradually increase our oil reserves and revenue base.

Yours Sincerely,



A. Stuart Cameron
President

North Continental Energy Ltd.

NOTICE OF ANNUAL MEETING

NOTICE OF ANNUAL GENERAL MEETING OF SHAREHOLDERS TO BE HELD THE 2nd DAY OF JUNE, 1988

TAKE NOTICE that on the aforesaid date, at the Magrath Room, Sven Ericksen's Family Restaurant, 1715 Mayor Magrath Drive, in the City of Lethbridge, in the Province of Alberta, at 2 o'clock in the afternoon, there will be convened a general meeting of all Shareholders of North Continental Energy Ltd. The meeting will consider the following:

1. The appointment of Munton/Anderson as Company auditors.

2. The meeting is also for the purpose of receiving and considering the reports of the Directors, the Auditor's report, the Financial Statements, the election of Directors and the transaction of any other business as may properly come before the meeting.

VOTING RIGHTS

3. Proxies in the form enclosed; which are properly executed, returned to management and not revoked; will be voted at such meeting in accordance with the authority contained therein. Any such proxy may be revoked before it is exercised.

4. 2,363,525 Common Shares without par value of the Company are outstanding each of which entitles the holder to one vote at all meetings of the Shareholders.

5. A shareholder has the right to appoint a person (who need not be a Shareholder) to attend and act for him on his behalf at the meeting other than the persons designated in the enclosed form of proxy. To exercise the right, the Shareholder may insert the name of the desired person in the blank space provided in the proxy or may submit another appropriate proxy. The proxy also confers discretionary authority with respect to amendments or variations to matters identified in the Notice of Meeting and other matters which may properly come before the meeting.

6. Those Shareholders desiring to be represented thereat by a nominee must deposit their proxies with the Corporate Secretary 48 hours prior to the commencement of the meeting.

SOLICITATION OF PROXIES

7. The costs of this solicitation of proxies for the Annual General Meeting of Shareholders are being borne by the Company. It is planned that the solicitation will initially be by mail but proxies may also be solicited by regular employees of the Company.

If you are unable to be present would you kindly sign, have witnessed and return the enclosed proxy. Dated at the City of Lethbridge, Alberta this 22nd day of April, 1988.

BY ORDER OF THE BOARD OF DIRECTORS

Donald R. Oliver, Secretary Treasurer

AUDITOR'S REPORT

To the Shareholders of
North Continental Energy Ltd.

We have examined the balance sheet of North Continental Energy Ltd. as at December 31, 1987 and the statements of income and retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the financial position of the company as at December 31, 1987 and the results of its operations and changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Munton/Anderson
Chartered Accountants

Lethbridge, Alberta
April 20, 1988

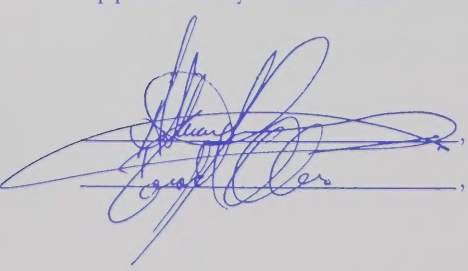
North Continental Energy Ltd.

BALANCE SHEET

December 31, 1987

	1987	1986
ASSETS		
CURRENT		
Cash	**$ 7,973**	$ —
Accounts receivable	**72,130**	103,592
Alberta Royalty Tax Credit	**37,266**	23,586
Income taxes recoverable	**—**	23,719
	117,369	150,897
INVESTMENTS (Note 2)	**843,899**	788,462
PROPERTY AND EQUIPMENT (Note 3)	**367,070**	381,325
	$1,328,338	$1,320,684
LIABILITIES		
CURRENT		
Bank indebtedness	**$ —**	$ 42,161
Accounts payable	**50,404**	21,623
Income taxes payable	**—**	14,188
	50,404	77,972
DEFERRED REVENUE (Note 4)	**79,357**	101,101
DEFERRED INCOME TAXES (Note 5)	**50,756**	42,661
SHAREHOLDERS' EQUITY		
SHARE CAPITAL		
Authorized		
20,000,000 common shares, no par value		
Issued		
2,363,525 common shares (Note 6)	**944,486**	929,486
CONTRIBUTED SURPLUS	**32,923**	32,923
RETAINED EARNINGS	**170,412**	136,541
	1,147,821	1,098,950
	$1,328,338	$1,320,684

Approved by the Board



_____, Director

_____, Director

North Continental Energy Ltd.

STATEMENT OF INCOME

Year Ended December 31, 1987

	1987	1986
REVENUE		
Interest	$ 3,575	$ 5,496
Natural gas and oil sales	131,886	106,801
Less: Royalties	(39,227)	(35,962)
Add: Alberta Royalty Tax Credits	37,266	23,586
Drilling grants	—	8,329
	133,500	108,250
EXPENSES		
Officers salary	15,000	30,000
Operating	20,331	16,375
General and administrative	17,714	18,399
Drilling costs	7,283	—
Depreciation and depletion	30,218	17,681
	90,546	82,455
Income before income taxes	42,954	25,795
Income taxes – current (recovered)	988	(23,719)
– deferred	8,095	42,661
	9,083	18,942
	$ 33,871	6,853

STATEMENT OF RETAINED EARNINGS

Year Ended December 31, 1987

	1987	1986
RETAINED EARNINGS, BEGINNING OF YEAR		
As previously reported	$ 136,541	$ 143,876
Prior period adjustment (Note 7)	—	(14,188)
As restated	136,541	129,688
NET INCOME	33,871	6,853
RETAINED EARNINGS, END OF YEAR	$ 170,412	$ 136,541

North Continental Energy Ltd.

STATEMENT OF CHANGES IN FINANCIAL POSITION

Year Ended December 31, 1987

	1987	1986
OPERATIONS		
Cash from Operations		
Net income	$ 33,871	$ 6,853
Add items not requiring funds (providing) funds		
Deprication	30,218	17,681
Deferred income taxes	8,095	42,661
	72,184	67,195
Net changes in non-cash working capital items related to operations (A)	56,094	(54,943)
	128,278	12,252
FINANCING		
Issuance of shares (net)	15,000	149,986
Repayment of debt (net)	(21,744)	(133,314)
Issuance of long term debt	—	52,434
	(6,744)	69,106
INVESTING		
Purchase of fixed assets	(15,963)	(198,339)
Purchase of investments	(55,437)	(16,590)
	(71,400)	(214,929)
INCREASE (DECREASE) IN CASH	50,134	(133,571)
CASH, BEGINNING OF YEAR	(42,161)	91,410
CASH, END OF YEAR	$ 7,973	$ (42,161)
(A) CHANGES IN WORKING CAPITAL ITEMS PROVIDING (REQUIRING) CASH		
Accounts receivable	$ 31,462	$ (46,352)
Alberta Royalty tax credit	(13,680)	17,113
Income taxes recoverable	23,719	(23,719)
Accounts payable	28,781	8,292
Income taxes payable	(14,188)	(10,277)
	$ 56,094	$ (54,943)

NOTES TO FINANCIAL STATEMENTS

December 31, 1987

1. ACCOUNTING POLICIES

North Continental Energy Ltd. is a public company which produces natural gas and oil and is incorporated under the Alberta Business Corporations Act. These financial statements are prepared in accordance with generally accepted accounting principles. The more significant accounting policies are:

Petroleum and Natural Gas Operations

The company capitalized the acquisition and exploration costs of both producing and non-producing leases and rights and changes such costs to earnings if the leases and rights are subsequently surrendered. The cost of drilling productive wells are capitalized and the cost of non-productive wells are charged to earnings when determined to be dry. The costs of producing wells including exploration, development and equipment thereon are amortized using the unit of production method based upon estimated quantities of oil and gas reserves.

Property and Equipment

Property and equipment are recorded at cost. Depreciation is calculated using the straight line method at the following rates:

Dehydration Plant	5%

Investments

Investments are recorded at cost.

Income Taxes

The Company records income taxes on the tax allocation basis. Under this method, income taxes relating to earnings currently recognized for accounting purposes but deferred for income tax purposes are fully provided for.

2. INVESTMENTS

	1987	1986
Barons Oil Limited: 302,500 shares at costs (market value 1987 – $877,250; 1986 – $840,420)	**$787,399**	$741,962
28% share of three Placer Claims	**56,500**	46,500
	$843,899	$788,462

3. PROPERTY AND EQUIPMENT

	1987			1986
	Cost	Accumulated Depreciation	Net Book Value	Net Book Value
Land	**$ 95,460**	**$ —**	**$ 95,460**	$ 88,665
Dehydration Plant	**166,346**	**79,761**	**86,585**	92,566
Natural Gas Wells	**113,729**	**15,558**	**98,171**	113,729
Non-Producing properties	**63,426**	**15,823**	**47,603**	85,324
Producing properties	**39,198**	**—**	**39,198**	—
Investment Tax Credits	**53**	**—**	**53**	1,041
	$ 478,212	**$ 111,142**	**$ 367,070**	$ 381,325

NOTES TO FINANCIAL STATEMENTS

December 31, 1987

4. DEFERRED REVENUE

Deferred gas revenue consists of amounts received under take-or-pay gas contracts and will be recognized as revenue when the related product is delivered to the purchaser.

5. DEFERRED INCOME TAXES

The deferred income taxes so provided result primarily from timing differences in the recording of depreciation and depletion of property and equipment for accounting purposes versus various allowances taken for income tax purposes.

6. SHARE CAPITAL

Shares issued to shareholders	1,976,025
Treasury shares	387,500
	$2,363,525

There are 2,355,480 shares of North Continental Oil and Gas Corporation Limited outstanding and are convertible to 588,870 shares of North Continental Energy Ltd.

During the year 30,000 shares were issued to senior management in lieu of salary. The 387,500 held in treasury are to be transferred to a trust for Senior Executive Stock Options.

7. PRIOR PERIOD ADJUSTMENT

As a result of income tax re-assessments applicable to the 1985 year, retained earnings and income taxes payable changed by $14,188 representing the total amount by which income taxes had been increased.

North Continental Energy Ltd.

OFFICERS OF THE COMPANY

A. STUART CAMERON
President

H. GORDON OLIVER
Vice President

DONALD R. OLIVER
Secretary Treasurer

DIRECTORS OF THE COMPANY

HOWARD H. OLIVER
Chairman of the Board

A. STUART CAMERON

H. GORDON OLIVER

NORMAN E. WADE

DONALD R. OLIVER

ANNUAL MEETING

2:00 p.m., June 2, 1988
Magrath Room, Sven Ericksen's Family Restaurant
1715 Mayor Magrath Drive
Lethbridge, Alberta

Printed in Canada

North Continental Energy Ltd.

1987 ANNUAL REPORT

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